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MEMORANDUM

To: Ken Lay, Grey Whalley, and Mark Frevert
From: Frank Luntz
Re: Initial Focus Group Observations & Recommendations
Date: October 19, 2001

OVERVIEW

The words I am about to write are direct, strong and may startle you but I am convinced of their accuracy.

I realize that at the end of the day, most of what I say here will be boiled down in terms of your bottom line: profitability and productivity. But that is *exactly* why you will hear me use words like *crisis* and *emergency*. From associates to VPs, your employees are telling us that these issues take up serious amounts of time during their workday. The negative environment they are working in has become more than just a distraction. It is now a barrier to the "excellence" and "performance" that Enron values so highly.

Having helped a number of large companies through similar problems, I can tell you firsthand that employees who are basically content with their jobs perform more efficiently and more effectively on a day-to-day basis. Employees who are frustrated at the levels we saw this week, tend to be less focused and less willing to give 110% when it matters most. So as I said before, this all comes down to your bottom line.

Your employees at the associate, manager, director and VP level made it very clear to us that they see a morale crisis among their colleagues at Enron. Sure, we live in unstable times, Enron prides itself on innovation and competition, and the precipitous drop in the stock price undoubtedly contributes to their expressions of insecurity and unease. But in listening to the four employee focus groups (stratified by level in the company), they are all waiting with growing impatience for senior management to provide a more clearly defined and less chaotic path toward the future.

The intensity and uniformity of responses cannot be dismissed. From systemic problems with HR to the lack of a corporate vision, there is a consensus at all four employee levels that Enron is at a crossroads and that the path you take in the coming months will determine whether you succeed in retaining and building a satisfied workforce or cause a mass exodus of employees.

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I must admit some surprise at how candid your employees were with me. I think one reason was that several people recognized me from my television work and that helped them realize that this was a serious effort to understand what employees really felt. But I must still emphasize that these are only "qualitative" results – a scientific quantitative survey will come later. We were looking for the kind of intensity and depth-of-response that only a focus group can deliver. And we certainly found it.

If you take only one thing away from this document, it should be this: ***your greatest asset and most powerful tool for communicating to employees is your CEO.*** Employees want to see Ken Lay's face. They want to hear from him and be led by him. Across the board, from associates to VPs, employees agree that ***in the midst of the employee crisis, any major initiative must be led by Ken if it is to have any chance of succeeding.***

You also know too well the impact that the stock price holds on employee morale. The problem is that there is still the nagging belief that the message delivered to "the street" is still different than the message delivered to employees. Yes, as the stock price rises, some employee dissatisfaction will dissipate. But there are also a number of other employee issues that ***are*** definitely under your control. And that is what I want to address here.

OBSERVATIONS

- (1) **Instability & Chaos:** We began each focus group by asking for a single word to describe Enron as a place to work. One theme stood out clearly above everything else: chaos, instability and uncertainty. In their own words, *"this can sometimes be a good thing, but most of the time it's dysfunctional and disorganized. The left hand doesn't seem to know what the right hand is doing."* In each group, it was very clear that this sense of instability is not a new phenomenon. Rather, for better and now for worse, it has become a part of the Enron culture.

No observation can illustrate the point more clearly than this: **of the 30 associate and manager-level employees we spoke to, 26 were actively planning or discussing their exit strategies from Enron.** Why? Most felt they had to. But this doesn't mean they *want* to. Of all the various options we offered employees that would better define the "excellence" of Enron, nothing scored better than the following statement: "working to make a place where employees stay for the long-run and build lasting relationships." Your employees simply feel that the possibility of a bad PRC review, having their business unit dissolve underneath them, or just plain bad (or lack of) corporate planning from the top down gives them little choice.

Not surprisingly, your VPs echoed the very same words we heard coming from your associates. They feel that *"there is a sense of chaos in our everyday work. It's a symptom of the lack of an overriding strategy at the top and it's starting to define practically everything."* They see this instability in their day-to-day work and they know that tensions are only getting worse.

- (2) **Reorganization:** Each of the four employee groups reacted to the number of "re-orgs" in much the same manner – with frustration and rolled eyes. Employees unanimously felt that the never-ending reorganization efforts not only makes communication difficult in the company, but it gives them little or no time to adjust or feel comfortable in their jobs. **Employees do understand the need to restructure the company and adjust to a changing market. But five or six reorganizations in an 18-month period are too many --** to the point that they are a major impediment to job performance.

This sentiment was echoed in all the groups. But it came up most loudly with the directors. "When you have five or six re-orgs in a year, it just leads to chaos. The managers need at least keep the re-orgs long enough to see results." In this manner, reorganization and instability are intricately linked.

- (3) **Waiting for the Roadmap:** At all levels of the company, employees are looking for a clear vision for the future of Enron and an understanding of their place in it. One of the VPs expressed the view that "as a company, we're still suffering from small-business syndrome. We're a major corporation still acting like a dot.com startup." But there is a positive side to this perception. Unanimously, employees want to hear that vision articulated. And they want to hear it from Ken Lay.

None of the employees seemed intimidated by new business opportunities. Most take great pride in the innovation and ingenuity of Enron. But they want to know that there is a "game-plan." Your VPs are particularly concerned that there appears to be no long term thinking, strategy or game plan from the corporate leadership. They want to know that their leaders have a path to follow. And they want their CEO to explain it to them.

- (4) **The Corporate Divide:** As a company, Enron recruits a special caliber of employee. People join Enron feeling they are truly the "best of the best." And most of them are. But it took only a matter of minutes to uncover the split between traders and everyone else. It took even less time to elicit the frustration that many employees have from seeing those same deal-makers put into managerial positions without any managerial experience whatsoever.

"Deal-makers do not necessarily make great leaders." This cliché was mentioned verbatim by each level of employee. Across the board, people felt that the deal-maker moved up the corporate ladder regardless of other abilities (or lack of) while implementers were too often forgotten. With a premium being placed on closing deals, most people feel that no one in the corporate leadership truly cares about those charged with executing the deals and making them actually produce profit.

This attitude came up most forcefully with your vice-presidents. It appeared to affect them most personally. They feel that *"there is no apparent reward for trying to be a team leader."* And this only makes their jobs more frustrating. With responsibility for improving morale largely on their shoulders, most feel it is *"utterly unrealistic"* to expect any real progress in the current environment.

- (5) **The PRC:** None of this is new to you but the intensity of this reaction cannot be overstated. I could very easily write an entire analysis on just the PRC and its effect on morale. It would start by saying that *you must be able to understand the PRC as your employees understand it.* At its heart, the PRC is seen as a *punitive* process, not an incentive policy. It is *not* viewed as a reward system. It is *not* viewed as a meritocracy. It is viewed as a punishment.

In addition to being seen as a penalty, the PRC is regarded as a highly politicized process that too often depends on the ability of a supervisor to defend his employees against the other members of the committee. As one employee put it: *"it all comes down to how good your manager is at defending you. I was told I had a pretty good score going in, but then the committee bumped me down and there was nothing he could do about it."* The extent of this frustration is best illustrated by our written exercises. **Among associates and managers, the number one step for improving morale is a PRC appeals process for employees who feel their assessments are unfair or biased.**

The PRC process also illustrates the level of disconnect between lower and upper-level employees. Among Associates, most in our groups did not know how the PRC actually worked. And even fewer had heard about the "Laying It On the Line" memo. Almost none of the associates understood the changes to the PRC that were taking place. In associates and managers alike, most wished their supervisors would explain the system better for them. But among directors and vice-presidents, there was a slightly clearer understanding of the process. Still, few were aware of the specific changes underway.

- (6) **Trust and the HR Department:** This is an important point because it highlights an interesting disconnect between middle-management and the rest of the staff. Among managers and directors, "an improved HR department where employees can have concerns acted upon without any fear of reprisal" was consistently ranked as a top step for improving morale. Among associates and vice-presidents, it was consistently at the bottom of the list.

Managers expressed repeated annoyance that their conversations with HR representatives were disclosed to others in the company. They were even more frustrated with the HR's inability to respond to problems and return phone calls in a timely manner. But these concerns are generally limited to middle management, perhaps because these are the people who deal most closely with HR on a day-to-day basis.

RECOMMENDATIONS

I offer these initial recommendations without the benefit of a scientific survey.
Please accept them as such:

- (1) **Take advantage of your most valuable asset – Ken Lay:** When it comes to all the key attributes in delivering a corporate message that your employees will believe and accept - credibility, confidence and trust -- Ken is your most powerful weapon. A personal commitment from Ken Lay will go further than the entire executive team combined. The VPs told us quite directly that *“any initiative, unless it is headed up and presented to the employees by Ken, will fail...absolutely.”*

This is not a warning. It is an opportunity.

Talk about positive change. Talk about employee morale in terms of where you will be five to ten years down the road. Talk about changes in terms of the innovation that has helped Enron in the past. When these words come from Ken, employees will listen.

But whatever you do, be very careful with where and how he focuses his message. The PRC is a classic example of the type of policy he should be staying away from. Employees associate the PRC with Jeff Skilling and the last thing you want is for that negative association to shift to Ken. So pick your messages very carefully.

- (2) **At every occasion, do not just write in a way that you will understand. Write so that your employees will understand you:** At first, this may seem like a vague recommendation. But I am putting it up front for a specific reason. It is integral to every other recommendation I can make. And the PRC is a good example of this point. Most of the employees who read the “Laying It On the Line” letter did not understand the changes discussed in it. Unfortunately, it was probably not home run that you were looking for.

Employees need to see side-by-side exactly how the system used to be and what specifically will be different from now on. Simply stated, they need a side-by-side explanation of the old and the new. And they needed to know how those changes will impact their everyday lives. That’s what I mean when I say *communicate in their terms, not yours.*

(3) **Memos must be backed up and reinforced by group discussions with immediate supervisors:** The disconnect between employees and their supervisors is striking up and down the corporate ladder. Focusing again on the PRC, any policy changes need to be followed-up with supervisors holding small staff meetings and explaining the changes that are happening. This is specifically what associates and managers asked for in the focus groups. They are less concerned with town-hall style meetings and Q & A sessions with their vice-presidents. But they do want an in-person explanation whenever major policies are being revised.

(4) **Compensate management for mandatory training sessions:** Associates criticize the lack of training in their supervisors and it is a source of daily frustration. As I have mentioned before, your employees are keenly aware that good deal-makers do not necessarily make good managers. Supervisors admit that what little training is offered is rarely taken seriously. If you want your managers to have the leadership skills necessary for doing their job, then training needs to be made a priority. And executives need to recognize and reward those who treat it as such.

(5) **Bring back employee mentoring and one-on-one "coaching" from senior employees:** Both associates and managers ranked this among their top choices for improving morale. They want greater access to their superiors. And they want the *cut-to-the-chase, no-nonsense* advice that only this sort of training can provide

Make no mistake, most associates will be happy to get whatever positive "face-time" they can get with their executives. But this is an opportunity to improve both training and communication in the same effort. Directors responded favorably to this idea and ranked it among their higher choices. And many of the VPs remembered similar policies from Enron's past. They expressed little adversity to getting involved and seemed willing to help their lower-level employees.

(6) **Consider a PRC appeals process to ensure fairness and accountability during reviews:** When it comes right down to it, nearly all your employees feel the same about the PRC process. They regard it as a biased system that is too often used for posturing rather than rewarding. If you intend to keep these reviews in place, something needs to be done to make them seem more systematic and less politicized.

This particular recommendation may not be the answer you go with in the end. But it is one that is regarded very favorably among all the employees we spoke to. Changing the criteria for review is seen as the best way to bring better accountability into the actual review process. When your employees regard the PRC system as an unfair tool used for penalizing, then a change needs to be made. And among associates and managers, this was their number one choice for doing so

- (7) **PRC restructuring must integrate the concept of teamwork:** This is a theme that came up several times in each focus group. Finally, the directors we were talking to insisted that we add the concept to one of our written exercises. When we did that, it was consistently ranked as the number one choice for improving employee morale. VPs voted unanimously that they want to see **“a significantly greater recognition of teamwork in the compensation process.”**

I realize that this is easier said than done. But employees at all levels feel that their team efforts are not being recognized in the PRC process. Non-traders feel that their abilities to implement and execute deals hold no weight during their performance reviews. Employees want these efforts recognized. They want credit for the teamwork that they believe is integral to Enron's success.

- (8) **Devote less time to online forums and e-solutions:** I do not know how much effort currently goes into maintaining these tools. But of the 56 employees we talked to, only 2 picked these efforts as something that demonstrates communication at Enron. My intention is not to attack these solutions. Employees showed no signs of being dissatisfied with their services. But there was little indication that online discussions were making a significant impression in either direction.

Quite frankly, they rarely came up at all. Only when we asked direct questions did employees mention them at all. None of them were ever mentioned by name. So what do they want instead? They want a personal statement from Ken Lay. They are not looking for chat-rooms and message boards. They want to actually see Ken and hear his voice. So some of that effort is probably better spent elsewhere.

- (9) **Create a significant PUBLIC effort to revitalize Enron's core values:** I am putting this recommendation last for a specific reason. We touched briefly on this idea during the wrap-up session following the focus groups. Frankly, this is a topic better discussed in person. Employees need something big to show them that things are truly different now at Enron. Too many feel they have been through this routine before. A major action/effort can go very far in showing employees that *real* changes are in effect and that things are really going to be different from now on.

One focus group participant commented that *“I've been in four employee morale discussions and nothing ever seems to change. Why should now be any different?”* You have an opportunity to show employees that their concerns are being taken seriously and acted upon. That sentiment has never existed before. It's a powerful message that will only come from taking an equally powerful stance.

CONCLUSION

After talking to and listening to employees at all levels of the company, I can safely say that I have never seen an employee disconnect so apparent that it actively turns the workplace into a negative environment. I realize that this is a harsh statement to make, but it is exactly what I'm hearing from your employees. And without a solution in place, that negativity tends only to feed on itself and get worse

Our focus groups showed us quite clearly that your employees are looking for leadership and a message from Ken Lay. They are waiting for that message and a clear plan of action. But they don't want just words. **They want actions to back up those words.** That is why some of my recommendations have been message oriented and others are tough policy solutions.

My goal here is not to make Enron employees love their jobs. But it is important that negativity and frustration be eliminated enough to turn the workplace back into the positive environment it should be. When you achieve that – and you certainly can – you will see performance levels increase across the board. That is why these issues are so important.

As I said in the beginning, these are based solely on what we are hearing in the focus groups. They are based on qualitative results...not polling numbers. The next step is to back up each recommendation with empirical data from the company as a whole. That will allow us to prioritize each step and produce a more concrete course of action

I look forward to that next step

A FEW WORDS FROM YOUR VPs
(apologies for the language but these are the exact words)

“Change is good. You can’t have too much change. But there needs to be stability in what people do.”

“What people are defining as chaos now we would probably have defined as creativity and entrepreneurship a year ago. But the bloom is off the lily right now ”

“The chaos is symptom of the lack of an operating strategy. Most people don’t think the top leadership have their shit together.”

“There is chaos in the company that starts at the top and filters down. There’s the feeling that we don’t follow our own bullshit.”

“It’s utterly unrealistic to maintain morale when the people above us don’t play the game properly.”

“If you look at people who made it to senior levels, they reflect the old Enron. You did it individually and you did it by making deals. We have a legacy of promoting people who were good individually but not necessarily as a team.”

“The Enron line, the verbiage that has nothing to do with how it is run. People are rewarded for all the wrong things.”

“I tell my guys how great things are. I say all the right things to them but in the back of my mind I know the truth.”

“Information travels around here so quickly. When our executive management says one thing and others know the truth, you get a problem. Look at today. People don’t feel like they’re getting the straight story right now, and the Street is sending back the same message.”

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Note: All nine VP participants defined the current employee situation as a crisis.